

# China's merger control regime in the face of global Integration: features and implications

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## Abstract

Since China's merger control regime under the Anti-Monopoly Law (AML) was established in 2008, the enforcement record has given rise to growing concern that the system is inherently biased against foreign multinationals. This article conducts an analysis of the evolution of China's merger review system to assess this charge and its implications. China's steady economic development fueled by foreign investment has led to a domestic market featuring strong foreign presence. Foreign-domestic competition figured as an important issue for the policymakers, especially in anticipation of China's entry into the WTO. This concern precipitated the establishment in 2003 of the country's first merger review system, which only applied to M&As by and between foreign companies. Although the AML on its face applies generally to both foreign and Chinese firms, enforcement authorities have only intervened in foreign takeovers. China's merger control regime is different from that of mature market economies and has significant implications for itself as well as foreign investors.

**Keywords:** China. Merger control. Global integration. Foreign-domestic competition

## 1 Introduction

Since China began to implement the Reform and Opening-Up Policy in 1978, it has engaged in an unprecedented undertaking of overhauling its legal system in order to facilitate and adapt to its stellar economic growth. Of the large

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number of changes and developments that have taken place in this area, the merger review system is a rather recent addition to China's legal infrastructure. In 2003 the *Provisional Regulations on Mergers with and Acquisitions of Domestic Enterprises by Foreign Investors* ("Provisional M&A Regulations") was adopted, containing in it a nascent antitrust mechanism to regulate only those M&As by and between foreign investors.<sup>2</sup> It was not until the *Anti-Monopoly Law* ("AML")<sup>3</sup> entered into force in August 2008, that China introduced a fully-fledged merger control regime that applies generally to both foreign and Chinese companies<sup>4</sup>.

From the beginning of its brief existence under the AML, however, China's merger review regime has been subject to close scrutiny and extensive debate. To a large extent this reflects the enormous interest in the AML generally, which, after 13 strenuous years of efforts to draft, is hailed as a significant landmark in China's gradual transition from central planning to a market economy. Merger review, together with provisions prohibiting cartels and abuse of dominant market position, constitute the three basic "pillars" of the AML. But more importantly, wide-spread public attention has been caused because authorities have taken an activist approach to merger enforcement that seemingly target foreign investors in particular. During two years after the merger review system was established under the AML, the enforcement agency approved six mergers subject to restrictive conditions and blocked one merger, all of which involved foreign multinational companies.

In developed market economies such as the U.S., antitrust regimes including merger review systems were established to address competition issues in a market composed almost exclusively of domestic firms. In contrast, under the bro-

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<sup>2</sup> ARTICLES 19-22. *M&A Regulations*. Available at: <<http://www.chinacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 17 Aug. 2010.

<sup>3</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau. *The anti-monopoly law of the people's Republic of China*, adopted by the 29th Session of the Standing Committee of the Tenth National People's Congress on 30 Aug. 2007, and promulgated by Presidential Order No. 68. Available at: <[http://www.gov.cn/ziliao/flfg/2007-08/30/content\\_732591.htm](http://www.gov.cn/ziliao/flfg/2007-08/30/content_732591.htm)>. Access on: 17 Aug. 2010.

<sup>4</sup> See Chapter VI of AML, which is entitled "control of concentrations". For the purpose of the discussion in this article, "merger control" is used interchangeably with "control of concentrations".

ad context of globalization and after more than two decades of rapid economic development fueled by international trade and foreign investment, China had very different market conditions and competition landscape when its first merger control legislation was adopted. Foreign dominance in many sectors posed formidable competitive threat to Chinese firms, while the government had long prioritized the expansion of domestic companies, especially the State-Owned-Enterprises (“SOEs”). Inevitably a major concern for the Chinese authorities is the foreign-domestic competition, which has remained an underlying policy issue during the entire development of China’s merger control system.

This article explores the features of China’s merger control regime and assesses its implications, in light of China’s integration with the world economy in the period of globalization. It reviews the historical background when the merger review component was first conceived, explains the early legislation of the merger review system, and provides an analysis of the existing merger review regime and law enforcement activities.

## **2 Background: the globalization impetus**

China’s accession to the WTO in 2001 started a new era for its integration into the rest of the world economy. As China’s market opened up further to the world, a legitimate concern arose about whether Chinese companies could compete with foreign firms, and whether China’s many fledging industries could fare well or even survive.

At the time, most Chinese business entities were still small and weak. Even China’s large, industrial companies were relatively small when put in the context of the global market. In 2002, China had only eleven firms listed in Fortune’s Global 500,<sup>5</sup> all of which operated under a protected domestic environment and enjoyed

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<sup>5</sup> SEE HU QIANGJIN: Eleven Chinese Firms on the Fortune Global 500 List, 20 jul. 2002. Available at: < <http://finance.sina.com.cn/g/20020720/234876.html>>. Access on: 30 Nov. 2010.

preferential treatment as large SOEs; half of them prospered as monopolies or oligopolies. Five of the biggest employers in the Global 500 were Chinese companies, which indicated serious inefficiency and downsizing problems. Furthermore, despite countless reform efforts, Chinese enterprises were still vulnerable to international competition in most sectors. No Chinese firm was qualified as a global giant corporation, and the daunting difficulties in SOE reform and economic transition seemed to continue to dim that prospect.

Due to China's WTO commitments, however, the large Chinese firms were soon to find themselves competing with multinational firms on a global level. China had promised to fully open up an array of protected sectors after relatively short grace periods. At the same time, because of global economic slowdown and China's steady growth, foreign companies had also intensified their efforts to penetrate the Chinese market. More than 400 of the Fortune Global 500 companies have made investments in China, and approximately 110 of them established study and design centers in China.<sup>6</sup> Two-thirds of the world's largest fifty retailers established business in China one year after China joined the WTO.<sup>7</sup> These are just a few examples of China's changing role in the multinational firms' global strategy: transition from merely a large potential market to the world's manufacturing factory. A few trends in foreign direct investment had confirmed this transition around 2001, including diversification of investment structure, localization of management and use of more advanced technology.<sup>8</sup> One notable change was the increase of wholly

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<sup>6</sup> SAN FENG. China's development: win-win instead of threat, *Jingji Can Kao bao*. 12 feb. 2003. Available at: <<http://www.people.com.cn/GB/jinji/36/20030212/921890.html>>. Access on: 15 Nov. 2010.

*Jingji Can Kao bao*. 12 feb. 2003. Available at: <<http://www.people.com.cn/GB/jinji/36/20030212/921890.html>>. Access on: 21 oct. 2010.

<sup>7</sup> SEE QIU JU. One year after accession to WTO (2002). *Working report by State Administration of Industry and Commerce of China*. Beijing, Issues 03, Feb. 2003.

<sup>8</sup> NEW trends in foreign investment in China by multinational companies. *Working paper of Ministry of Foreign Trade and Economic Cooperation*. Beijing, Issues 11, Jul. 2002.

foreign-owned enterprises and decrease of joint ventures.<sup>9</sup> Foreign investors were also showing a growing interest in mergers and acquisitions as a channel for expansion rather than joint ventures since 2002. This was clearly an indication of foreign firms' elevated confidence in their long-term presence in China.

Chinese leaders were fully aware of the double-edged nature of the foreseeable intensification of competition in China's home market. While policy makers had counted on competition to improve the performance of domestic firms and boost economic growth, they were increasingly concerned that foreign firms might "muscle in" too swiftly and become monopoly powers before the Chinese enterprises were well-established. Foreign conglomerates with superior technical expertise, efficient management and ample capital possessed a formidable power sufficient to crush many of China's fledgling industries. Early signs had given some foundation to this fear. Foreign companies already dominated the markets of computers, cables, sedan cars, rubber, switchboards, beer, paper, elevators, pharmaceuticals, and detergent, among other products.<sup>10</sup> In some areas mergers and acquisitions with the purpose of obtaining a larger market share were noted.<sup>11</sup>

In anticipation of WTO obligations to reduce trade barriers, China recognized the importance of putting into place a viable legal mechanism to address competition ramifications. In October 2001, on the eve of the WTO accession, the Chinese government pledged to enact or revise "a series of laws in compliance with WTO rules to preserve fair competition and protect domestic industries," including specifically an anti-monopoly law.<sup>12</sup> Other rules included on this list, the *Anti-Dum-*

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<sup>9</sup> According to Ministry of Foreign Trade and Economic Cooperation statistics, joint-equity ventures decreased 4.74% in 2002 from the previous year and cooperative joint ventures dropped 18.59%, while wholly foreign-owned enterprises increased by 32.87%. There were 22,173 newly-established, wholly foreign-owned enterprises in 2002, comprising 65% of the 34,171 newly-established FDI enterprises that year.

<sup>10</sup> LU JIONG XING (ed.). *Studies of China's foreign investment law*. Beijing: China Law Press, 2001. p. 167.

<sup>11</sup> For example, Kodak's merger with two Chinese firms in 1998 led to its 70% market share in film products in 2001.

<sup>12</sup> STATE economic & trade commission: guidelines of the industry structure adjustment for the tenth five-year plan. oct. 2001. Available at: <[http://code.fabao365.com/law\\_248738\\_1.html](http://code.fabao365.com/law_248738_1.html)>. Access on: 30 Nov. 2010.

ping, *Anti-Subsidy and Safeguard Regulations* were enacted shortly afterwards,<sup>13</sup> which China prepared itself to use fully whenever possible.<sup>14</sup> The envisioned anti-monopoly law, with fundamental and far-reaching implications for competition and market order, had thus become a top priority on the legislative agenda.

### 3 The embryonic stage: wariness toward foreign acquirers

As early as 1987, a working group on drafting the anti-monopoly law was established under the Legislative Affairs Bureau of the State Council. In 1994, the 8th National People's Congress included the anti-monopoly law in its legislative plan. However, the drafting of an entire package of law met with great difficulty due to the many controversial issues involved, particularly those on state monopolies and government distortion of market competition.

When WTO membership raised pressing concerns on foreign competition, the Chinese decision-makers seemingly sought to address this immediate issue in part by introducing first a merger control scheme that only regulated M&A activities of foreign investors. This was done by quietly inserting four articles in the 2003 Provisional M&A Regulations.<sup>15</sup> The passage of the Provisional M&A Regulations, a departmental regulation, was much easier than that of a comprehensive anti-monopoly statute. Contained in a set of foreign investment provisions those articles were also inconspicuous, until the adoption of the 2006 amended M&A Regulations, in which the four articles essentially remained unchanged but formed a separate and distinctive chapter entitled "anti-monopoly review".

Despite of such a modest start in terms of legislation, the four articles by themselves constituted a sufficiently operational merger control regime that was shortly put into implementation. Notably this scheme was largely independent

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<sup>13</sup> The three regulations were adopted on 31 oct. 2001 and became effective on 1 jan. 2002.

<sup>14</sup> YOUNGJIN JUNG. China's aggressive legalism. China's First Safeguard Measure. *Journal of World Trade*, Netherlands, v. 36, n. 6, 2002. p. 1037-1060.

<sup>15</sup> ARTICLES 19-22. *M&A Regulations*. Available at: <<http://www.chinaacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 Nov. 2010.

from the M&A Regulations, to which it was built into. The other provisions in this regulation set out regulatory requirements and procedures regarding only M&As by foreign investors of domestic firms in China, while the merger review rules applied to both those transactions and offshore M&As that affected Chinese market. The latter obviously fell outside the stated scope of the M&A Regulations, but in practice it turned out that they made up the majority of transactions notified to the authorities.

Two central government agencies, Ministry of Foreign Trade and Economic Cooperation (“MOFTEC”) and State Administration for Industry and Commerce (“SAIC”) shared enforcement jurisdiction according to the regulation.<sup>16</sup> But shortly afterwards, before MOFTEC allocated staff to this work, it was replaced by the Ministry of Commerce (“MOFCOM”) following a government reorganization. For the same transaction, notifying parties normally submitted identical documents to both agencies. Each conducted review and investigation separately without consulting or coordinating with each other. Merger review process was considered complete when both authorities had made their decisions.

Respective notification thresholds were established for M&As inside and outside China. For transactions inside China involving foreign investors acquiring domestic firms, if any of the following conditions were met, the investors should notify MOFCOM and SAIC: (1) the annual turnover of one party in the Chinese market exceeds RMB 1.5 billion; (2) more than 10 firms in relevant industries in China have been acquired within one year; (3) one party has a market share of at least 20% in China; and (4) as a result of the transaction, the market share of one party reaches 25% in China. In addition, even if those thresholds were not met, whenever the enforcement agencies considered it necessary due to concerns of large markets share, market competition or national economic security, they had the power to request notification by the foreign investors.<sup>17</sup>

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<sup>16</sup> ARTICLES 19-22. *M&A Regulations*. Available at: <<http://www.chinaacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 Nov. 2010.

<sup>17</sup> ARTICLE 19. *M&A Regulations*. Available at: <<http://www.chinaacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 Nov. 2010.

With respect to offshore M&As, in addition to the above (1) (3) and (4) thresholds, two other rules also applied: either the total asset value of one party in China exceeds RMB 3 billion; or as a result of the transaction, one party is to have shareholding in more than 15 firms in relevant industries inside China.<sup>18</sup>

At the same time, notifiable transactions could be exempted from merger review for the following benefits that might ensue: (1) improvements of conditions for market competition; (2) restructure of failing firms and contribution to employment; (3) introduction of advanced technology and managerial expertise, and enhancement of firms' international competitiveness; and (4) environmental improvements.<sup>19</sup>

Substantive standards were given for enforcement agencies to take into consideration in conducting reviews and making decisions, although they were in rather general terms such as over-concentration, fair competition, consumer welfare, and national economic security.<sup>20</sup> There were only a few procedural rules, such as that a decision should be made within 90 days after a complete notification was filed, and within that period the two enforcement agencies could jointly or independently hold hearings and invite participation of relevant government agencies, entities, companies or other stakeholders.<sup>21</sup> To put those broad and simple rules into implementation, MOFCOM adopted a *Guideline of for Anti-monopoly Filing for Mergers with and Acquisitions of Domestic Enterprises by Foreign Investors*

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<sup>18</sup> ARTICLE 21. *M&A Regulations*. Available at: <<http://www.chinacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 Nov. 2010.

<sup>19</sup> ARTICLE 22. *M&A Regulations*. Available at: <<http://www.chinacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 Nov. 2010. ARTICLES 19-22. *M&A Regulations*. Available at: <<http://www.chinacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 nov. 2010.

<sup>20</sup> ARTICLES 19, 20. *M&A Regulations*. Available at: <<http://www.chinacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 Nov. 2010. ARTICLES 19-22. *M&A Regulations*. Available at: <<http://www.chinacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 nov. 2010.

<sup>21</sup> ARTICLE 22. *M&A Regulations*. Available at: <<http://www.chinacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 Nov. 2010. ARTICLES 19-22. *M&A Regulations*. Available at: <<http://www.chinacc.com/new/63/159/177/2006/1/wa333914728211600220049-0.htm>>. Access on: 15 Nov. 2010.



(“Filing Guideline”) with detailed procedural requirements.<sup>22</sup> Although the Filing Guideline was not legally binding in nature, it provided much-needed guidance and predictability for notifying parties and in practice was generally followed.

The major weakness of this merger control system is the lack of enforcement power possessed by the agencies. The regulation itself was silent as to liabilities for failing to notify a reportable transaction or non-compliance with a decision by the agencies to block a deal. Moreover, as merger review was an entirely new component to the Chinese legal system, there was no other legislation to which reference could be made. From its establishment in 2003 until 2008 before AML became effective, more than 600 merger notifications were filed with MOFCOM and SAIC.<sup>23</sup> All decisions ever handed down were clearances and therefore officially no transaction was prohibited. However, not all transactions were rubber-stamped either. For example, in the high-profile Carlyle/*Xugong* acquisition, in which Carlyle Group, the U.S. private equity firm, initially agreed to acquire 85% of equity in *Xugong* Machinery, parties finally abandoned the transaction when they failed in their three-year efforts to obtain a clearance through several revisions of their agreements proposing decreases of the to-be-acquired share percentage.<sup>24</sup>

## **4 Merger control under the AML: foreign competition still the focal point**

### **4.1 The framework**

The AML establishes a comprehensive merger control regime that no longer in itself differentiate between foreign and domestic parties. In fact it has been repeatedly emphasized by the authorities that the AML shall be uniformly and

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<sup>22</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Available at: <<http://www.winkinglaw.com/ResourceFolder/200873012145256.pdf>>. Access on: 15 Nov. 2010.

<sup>23</sup> SHANG MING. *Government online interview: improving antimonopoly enforcement and safeguarding fair market competition*. 2008. Available at: <<http://www.gov.cn/zxft/ft155>>. Access on: 15 Nov. 2010.

<sup>24</sup> CARLYLE’S proposed stake acquisition in xugong falls through. Available at: <<http://www.chinastakes.com/2008/7/carlyles-proposed-stake-acquisition-in-xugong-falls-through.html>>. Access on: 15 Nov. 2010.

equally applicable to both domestic and foreign enterprises of any nature without any discriminatory treatment.<sup>25</sup>

MOFCOM was designated as the only enforcement agency for merger control under the AML.<sup>26</sup> An Anti-Monopoly Bureau (“AMB”), consisting of 6 divisions, was established under MOFCOM in September 2008 to perform this function. In addition to handling merger cases, the AMB is also responsible for drafting implementing regulations, rules and guidelines of the AML provisions on merger control. Several such documents have been adopted, including the *Guidelines on the Definition of Relevant Market*<sup>27</sup> and the *Measures on the Review of Concentrations between Undertakings*<sup>28</sup>, contributing the continuous expansion and evolution of the merger control system.

As foreshadowed by the AML<sup>29</sup>, on August 3, 2008, the State Council adopted the *Provisions of the Pre-Notification Thresholds for Concentrations between Un-*

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<sup>25</sup> HARRIS JR, H. Stephen; SHUGARMAN, Keith D *Interview with Shang Ming*, director general of the anti-monopoly bureau under the ministry of commerce of the people’s Republic of China. Available at: <<http://www.abanet.org/antitrust/at-source/09/02/Feb09-ShangIntrvw2-26f.pdf>>. Access on: 15 Nov. 2010.

<sup>26</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau. Pursuant to the “three designation plan” approved by the state council, MOFCOM is responsible for conducting review of concentrations between undertakings in accordance with the law. See the description of the function of MOFCOM Anti-Monopoly Bureau on its official website. Available at: <<http://fldj.mofcom.gov.cn/aarticle/gwym/200809/20080905756026.html>>. Access on: 18 Nov. 2010. See also THE measures on the notification of concentrations of undertakings, *MOFCOM order*, 2009. Available at: <<http://fldj.mofcom.gov.cn/aarticle/c/200911/20091106639149.html>>. Access on: 18 Nov. 2010.

<sup>27</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau. *News release*. Available at: <<http://fldj.mofcom.gov.cn/aarticle/j/200907/20090706384131.html>>. Access on: 18 Nov. 2010.

<sup>28</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau. *News release*. Available at: <<http://fldj.mofcom.gov.cn/aarticle/c/200911/20091106639145.html>>. Access on: 18 nov. 2010.

<sup>29</sup> ARTICLE 21. *The anti-monopoly law of the people’s Republic of China (AML)*. Available at: <[http://www.gov.cn/ziliao/flfg/2007-08/30/content\\_732591.htm](http://www.gov.cn/ziliao/flfg/2007-08/30/content_732591.htm)>. Access on: 17 Aug. 2010.

*undertakings*<sup>30</sup>, setting up a new set of notification thresholds. According to Article 3, no merger shall be implemented without prior notification if they reach either of the following thresholds: (1) the aggregate worldwide sales revenue during the previous fiscal year of all undertakings participating in the concentration exceeds RMB 10 billion, and each of at least two of such undertakings' sales revenue in China during the previous fiscal year exceeds RMB 400 million; (2) the aggregate sales revenue in China during the previous fiscal year of all undertakings participating in the concentration exceeds RMB 2 billion, and each of at least two of such undertakings' sales revenue in China during the previous fiscal year exceeds RMB 400 million.<sup>31</sup>

Upon the receipt of a complete notification pursuant to Articles 23 and 24, MOFCOM initiates a 30-day preliminary review.<sup>32</sup> If the agency decides that further review is warranted, the investigation will move into second stage, subject to a time limit of 90 days and a possible extension of up to another 60 days.<sup>33</sup> In conducting substantive evaluation of the merger, the following factors should be considered: (1) market shares of parties and their controlling power over the market; (2) the degree of market concentration; (3) the impact of the concentration on market access and technological progress; (4) the impact of the concentration on consumers and other undertakings; (5) the impact of the concentration on national economic development; and (6) other elements that affect competition and should be taken into account.<sup>34</sup>

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<sup>30</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau. *News release*. Available at: <<http://fldj.mofcom.gov.cn/aarticle/c/200811/20081105917434.html>>. Access on: 18 Nov. 2010.

<sup>31</sup> At the same time, Article 4 provides that: "where a concentration of undertakings does not reach any of the thresholds specified in Article 3 of these Provisions, but facts and evidence collected in accordance with the prescribed procedures establish that such concentration effects, or is likely to effect, the elimination or restriction of competition", the enforcement agency shall initiate an investigation in accordance with law.

<sup>32</sup> ARTICLE 25. *AML*. Available at: <[http://www.gov.cn/ziliao/flfg/2007-08/30/content\\_732591.htm](http://www.gov.cn/ziliao/flfg/2007-08/30/content_732591.htm)>. Access on: 17 Aug. 2010.

<sup>33</sup> ARTICLE 26. *AML*. Available at: <[http://www.gov.cn/ziliao/flfg/2007-08/30/content\\_732591.htm](http://www.gov.cn/ziliao/flfg/2007-08/30/content_732591.htm)>. Access on: 17 Aug. 2010.

<sup>34</sup> ARTICLE 27. *AML*. Available at: <[http://www.gov.cn/ziliao/flfg/2007-08/30/content\\_732591.htm](http://www.gov.cn/ziliao/flfg/2007-08/30/content_732591.htm)>. Access on: 17 Aug. 2010.

The AML makes clear that after its assessment of the merger the enforcement agency can take a decision to clear a merger, to conditionally approve a merger or to prohibit a merger.<sup>35</sup> Decisions prohibiting a merger or attaching restriction conditions to a merger should be published in a timely manner.<sup>36</sup>

Legal liabilities for violations of the merger review provisions under the AML are specified. If a merger is implemented in violation of the law, the enforcement agency shall order the parties to cease the implementation of the transaction, order the divestment of the shares or assets or the transfer of business operations within a given time limit, and take other measures necessary to restore the conditions prevailing before the closing. In addition, it may impose a fine of up to RMB 500,000.<sup>37</sup>

## 4.2 Cases

Since the AML merger control regime was established in August 2008, MOFCOM has taken an activist approach to merger enforcement. During a period of two years, the enforcement agency approved six mergers subject to restrictive conditions and blocked one merger. The seven decisions, all published pursuant to AML requirement, bear strong testimony to the increased enforceability of the merger review regime compared to the previous system, most importantly due to the introduction of provisions on the decisions MOFCOM can take and legal liabilities for violations.

However, although the AML merger review no longer limits its application to only transactions involving foreign acquirers, actual enforcement activities seem to suggest that those are still the foremost concern of the Chinese authorities.

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<sup>35</sup> ARTICLE 29. *AML*. Available at: <[http://www.gov.cn/ziliao/flfg/2007-08/30/content\\_732591.htm](http://www.gov.cn/ziliao/flfg/2007-08/30/content_732591.htm)>. Access on: 17 Aug. 2010.

<sup>36</sup> ARTICLE 30. *AML*. Available at: <[http://www.gov.cn/ziliao/flfg/2007-08/30/content\\_732591.htm](http://www.gov.cn/ziliao/flfg/2007-08/30/content_732591.htm)>. Access on: 17 Aug. 2010.

<sup>37</sup> ARTICLE 48. *AML*. Available at: <[http://www.gov.cn/ziliao/flfg/2007-08/30/content\\_732591.htm](http://www.gov.cn/ziliao/flfg/2007-08/30/content_732591.htm)>. Access on: 17 Aug. 2010.

All the seven decisions, as illustrated below, focus on addressing potential negative impact as a result of M&As by and between foreign companies.

#### **4.2.1 InBev/Anheuser-Busch**

On November 18, 2008, MOFCOM decided to grant a qualified approval of InBev's acquisition of Anheuser-Busch with certain restrictive conditions attached.<sup>38</sup> InBev was a global brewer in Belgium and Anheuser-Busch was a leading U.S. beer manufacturer. Both had shares in certain Chinese beer producers at the time.

The *InBev/Anheuser-Busch* decision is the first conditional approval given by MOFCOM in its review of mergers since 2003, and the first decision ever published. The restrictive conditions include that the 27% equity interest currently held by Anheuser-Busch in Tsingdao Brewery shall not be increased; any change to InBev's controlling shareholder or any change to the shareholders of such controlling shareholder shall be promptly notified to MOFCOM; the 28.56% equity interest currently held by InBev in Zhujiang Beer shall not be increased; and no effort or attempt shall be made to acquire any shares in China Resources Snow Brewery or Beijing Yanjing Brewery.

In a short announcement by MOFCOM the purpose for those restrictive conditions is clearly stated to be "to mitigate any adverse impact that may *possibly* arise on *future* competition in the Chinese beer market"<sup>39</sup>, due to the "large size of the merger" and given the "high market share" and "substantially increased competitiveness" of the merged entity. Investigation findings, indicated by the announcement and confirmed in the an interview with Director General of AMB ("InBev

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<sup>38</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau *MOFCOM public notice*. Available at: <<http://fdj.mofcom.gov.cn/aarticle/ztxx/200811/20081105899216.html>>. Access on: 18 Nov. 2010.

<sup>39</sup> Emphasis added.

Interview”)<sup>40</sup>, are that the merger does not eliminate or restrict competition in the Chinese beer market.<sup>41</sup>

In other words, as a threshold issue, no harm to competition is identified in this case. Rather, the authorities are concerned about possible “future” harm that may materialize only upon further expansion of the merged firm through increase of control in China’s major beer manufacturers. It is explained that MOFCOM considers those restrictive conditions necessary to pre-empt the potential emergence of anticompetitive market structure as a result of the merger.<sup>42</sup> If increase of market share alone is taken as the negative effect on competition, it is inconsistent with MOFCOM’s view that growth of company in itself is not considered anticompetitive.<sup>43</sup> Implicitly, anticompetitive market structure here refers to one in which the growth of foreign companies squeeze out domestic competitors.

#### 4.2.2 Coca Cola/Huiyuan

On March 18, 2009, MOFCOM announced its decision to reject the proposed bid by Coca Cola Corp of the entire shares of Huiyuan Juice Group, the largest juice maker and a household brand in China.<sup>44</sup> Among the seven cases, this is the

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<sup>40</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau *The InBev interview*. Available at: <<http://fldj.mofcom.gov.cn/aarticle/zcfb/200812/20081205935637.html>>. Access on: 18 Nov. 2010.

<sup>41</sup> The decision only states that the merger is “not prohibited in accordance with Article 28 of AML.” But in the InBev interview, DG Shang Ming explained that “[...] as investigation findings show that this merger does not have the effect of eliminating or restricting competition in the Chinese beer market, MOFCOM has decided not to prohibit it [...]”

<sup>42</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau *The InBev interview*. Supra note 40. Available at: <<http://fldj.mofcom.gov.cn/aarticle/zcfb/200812/20081205935637.html>>. Access on: 18 nov. 2010.

<sup>43</sup> At the end of the InBev Interview, DG Shang Ming emphasized that “the purpose of the anti-monopoly review of concentrations between undertakings is not to curb the growth of enterprise size, but to avoid the anticompetitive effects resulting from such size increase [...]” See supra note 40.

<sup>44</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau *MOFCOM public notice*. Available at: <<http://fldj.mofcom.gov.cn/aarticle/ztxx/200903/20090306108494.html>>. Access on: 18 Nov. 2010.

only one that involves a contemplated takeover by a foreign company of a Chinese firm, and so far it remains the only merger that has been blocked by MOFCOM.

MOFCOM's decision was based on affirmative findings of negative effects that the merger would cause. Firstly, it was concerned that the acquisition of Huiyuan would enable Coca Cola to leverage its dominant position in the carbonated soft drinks market into the juice beverage market. Secondly, the control of two well-known brands ("Minute Maid" and "Huiyuan"), in addition to Coca Cola's dominant position and the leverage effect, would raise entry barriers to the juice beverage market to potential competitors. Thirdly, the acquisition would squeeze out smaller juice manufactures in China, restrain the abilities of local producers to participate in competition and innovation in the juice market, and therefore harm the competition in the Chinese juice beverage market and undermine its sustained and healthy development.

Although the decision refers to "consumer welfare" and "entry barrier", it elaborates more on concerns relating to domestic firms in its reasoning. Although remedy proposals had been first discussed, eventually none were accepted by MOFCOM as sufficient to address those identified concerns.

#### **4.2.3 Mitsubishi Rayon/Lucite**

On April 24, 2009, MOFCOM announced its decision to conditionally approve Japanese chemical giant Mitsubishi Rayon's planned purchase of British-based Lucite.<sup>45</sup> According to the decision, the proposed transaction would give the merged entity a combined share of 64% in the Chinese methyl methacrylate ("MMA") market, significantly larger than those of its competitors. MOFCOM was concerned that the dominant position would enable the merged firm to eliminate or restrict competitors in China's MMA market. In addition, as Mitsubishi Rayon

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<sup>45</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau *MOFCOM public notice*. Available at: <<http://fldj.mofcom.gov.cn/aarticle/ztxx/200904/20090406198805.html>>. Access on: 18 Nov. 2010.

also operates in two downstream markets of MMA, the dominance in the MMA market would likely cause foreclosure effects and restrict access to MMA by downstream competitors of the merged entity.

To address those concerns, MOFCOM decided to impose certain conditions, including: Lucite's Chinese subsidiary, Lucite China is required to divest 50% of its annual MMA production capacity for five years; the China operations of Lucite China's and Mitsubishi Rayon's MMA businesses must be managed separately, from the closing of the proposed transaction to the completion of the divestiture; and for five years from the closing of the transaction, the merged entity may not acquire producers or build new plants in China that manufacture MMA monomer, PMMA polymer, or cast sheet products, absent MOFCOM's prior approval.

In contrast to the *InBev/Anheuser-Busch* case, this decision is based on affirmative findings of adverse effects of the merger on competition in the Chinese market. However, the decision offers no explanation about how the imposed conditions, for example the divestiture of 50% of Lucite China's production capacity for a period of five years, can "adequately cure"<sup>46</sup> the anticompetitive impact of the transaction. As with the *InBev/Anheuser-Busch* decision, it also seeks to control future strategic activities by the merged entity. The effects of those conditions appear to be similar to that of *InBev/Anheuser-Busch*, that is, to restrict the growth of foreign competitors. Only that in this case the restriction has a term of five years.

#### **4.2.4 GM/Delphi**

On September 28, 2009, MOFCOM conditionally approved the proposed acquisition of Delphi by General Motors ("GM"), a transaction involving two U.S.

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<sup>46</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau *MOFCOM public notice*. Paragraph 7. Available at: <<http://fdj.mofcom.gov.cn/article/ztxx/200904/20090406198805.html>>. Access on: 21 Nov. 2010.



companies.<sup>47</sup> Considering “GM’s leading position in the global and Chinese automobile manufacture markets, and the leading position and growth of Delphi in the global and Chinese auto parts markets”, MOFCOM stated concerns that the merger would be likely to eliminate or restrict competition in the Chinese automobile market and its upstream auto parts market.<sup>48</sup>

MOFCOM decided to clear the merger subject to the following restrictive conditions: the parties must ensure the stability, price and quality of supply to other domestic automakers supplied by Delphi; Delphi may not disclose to GM any competitive confidential information of other domestic automakers, and the parties may not exchange competitive confidential information of third parties; Delphi will assist in the smooth switching of suppliers by its customers; and GM must continue to procure auto parts from multiple sources on a non-discriminatory basis and must not unreasonably favor Delphi over its competitors.

Car manufacturing in China is a protected industry dominated by SOEs and foreign shareholding in any joint venture in this industry cannot exceed 50%. The decision clearly attempts to protect domestic automakers against any potential anticompetitive behavior by the merger entity.

#### **4.2.5 Pfizer/Wyeth**

On September 29, 2009, a fourth clearance decision was delivered concerning a transaction between two U.S. pharmaceutical companies, the proposed acquisition of Wyeth by Pfizer.<sup>49</sup> MOFCOM concluded that the merger would raise

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<sup>47</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau *MOFCOM public notice*. Paragraph 7. Available at: <<http://fdj.mofcom.gov.cn/aarticle/ztxx/200909/20090906540211.html>>. Access on: 21 Nov. 2010.

<sup>48</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau *MOFCOM public notice*. Paragraph 7. Available at: <<http://fdj.mofcom.gov.cn/aarticle/ztxx/200909/20090906540211.html>>. Access on: 25 Nov. 2010.

<sup>49</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau *MOFCOM public notice*. Available at: <<http://www.mofcom.gov.cn/aarticle/b/c/200910/20091006544714.html>>. Access on: 28 Nov. 2010.

competition concerns on the market for swine mycoplasma pneumonia vaccine in China. According to the decision, the two parties would hold a market share of 49.4% after the merger, significantly higher than that of any other competitor. As a result, the merged company would be capable of taking advantage of its scale and control product prices.

MOFCOM therefore required that Pfizer fulfill the following obligations as conditions to approve the merger: Pfizer must divest identified swine mycoplasma pneumonia vaccine business in the Chinese domestic market subject to procedural requirements and time limits set by MOFCOM; the business to be divested includes tangible and intangible assets that are necessary for the viability and competitiveness of such business; and within three years of the divestment and upon the buyer's request, Pfizer has the obligation to provide the buyer with reasonable technical support and related assistance.

The *Pfizer/Wyeth* decision seems to repeat the presumption that a high market share automatically leads to a dominant position, which is the primary basis for a finding of anticompetitive effects.

#### **4.2.6 Panasonic/Sanyo**

On October 30, 2009, MOFCOM granted conditional clearance for the proposed acquisition of Sanyo by Panasonic, two Japanese firms.<sup>50</sup> Through its review, MOFCOM determined that the acquisition would harm competition on three already highly concentrated battery markets because both parties had a high market share leading to a dominant position in these markets.

According to the decision, the merging parties are obliged to divest a significant portion of their existing businesses relating to the three markets. They are

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<sup>50</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau *MOFCOM public notice*. Available at: <<http://fdj.mofcom.gov.cn/aarticle/zcfb/200910/20091006593175.html>>. Access on: 28 Nov. 2010.

required to find independent buyers for those assets to be divested, and must find the qualified purchasers within six months upon MOFCOM's approval, with a possible extension for another six months, again subject to MOFCOM's approval. In addition, Panasonic committed to reducing its shareholding in a Panasonic-Toyota joint venture from 40% to 19.5% and relinquish certain management rights in the joint venture.

Unlike the previous decisions, in which the relevant geographical market is explicitly or implicitly defined as the Chinese market, this case set the analysis in the context of the world market, and most of the businesses to be divested in this case are in Japan. It does not specify to what degree the proposed transaction would negatively affect the Chinese market and how the restrictive conditions will remedy it.

#### **4.2.7 Novartis/Alcon**

On August 13, 2010, MOFCOM conditionally approved the proposed acquisition by Swiss pharmaceutical company Novartis of Alcon, a global medical company specializing in eye care products that is also incorporated in Switzerland.<sup>51</sup>

MOFCOM found that the transaction may have the effect of eliminating or restricting competition in ophthalmic anti-inflammatory/anti-infective compounds market and contact lens care markets, due to high or leading combined market shares. To address those concerns, MOFCOM and the notifying parties agreed on two remedy measures, that Novartis is required to cease sales of its own anti-inflammatory/anti-infective compounds products in China by the end of 2010 and the restriction will last for 5 years from the date of the decision; and Novartis must terminate its strategic partnership with *Haicheng*, which has the biggest market share of contact lens care products in China, within 12 months of the decision.

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<sup>51</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau. *MOFCOM public notice*. Available at: <<http://fdj.mofcom.gov.cn/aarticle/ztxx/201008/20100807080639.html>>. Access on: 28 Nov. 2010.

Notably, the requirement that Novartis withdraw its anti-inflammatory/anti-infective eye-care products from the China market was made despite the fact that Novartis had a very small market share, admittedly less than 1%, in the relevant market. In addition, Novartis had already committed, as part of the transaction, to effect such a withdrawal. With no explanation offered in the decision, the justification for MOFCOM's concerns can be questionable.

## 5 Concluding remarks

In a press conference to commemorate the two-year anniversary of the AML in relation to the enforcement work of MOFCOM, <sup>52</sup>the Director General of AMB reiterated the agency's position that AML applies non-discriminatorily to SOEs, private firms and foreign companies alike.<sup>53</sup> Ironically, the very next day, MOFCOM published yet another and the latest conditional clearance decision in *Novartis/Alcon*, which only added to doubts that the enforcement agency has particularly targeted foreign companies. Of the more than 140 notifications that MOFCOM received during the first two years after the AML entered into force,<sup>54</sup> all but seven were unconditionally cleared. The single prohibition decision concerned a foreign takeover of the largest domestic player in the relevant market, while all the six conditional clearance decisions applied to M&As outside China between foreign multinationals.

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<sup>52</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau. *The news report of this news conference*. Available at: <<http://fldj.mofcom.gov.cn/aarticle/xxfb/201008/20100807077394.html>>. Access on: 28 Nov. 2010.

<sup>53</sup> CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau. The transcript of the questions and answers during this press conference. Available at: <[http://www.gov.cn/gzdt/2010-08/12/content\\_1678211.htm](http://www.gov.cn/gzdt/2010-08/12/content_1678211.htm)>. Access on: 28 Nov. 2010.

<sup>54</sup> The latest reported statistics show that as of June 2010, MOFCOM received more than 140 notifications.

CHINA. Ministry of Commerce of the People's Republic of China. Anti-monopoly Bureau. The transcript of the questions and answers during this press conference. Available at: <[http://www.gov.cn/gzdt/2010-08/12/content\\_1678211.htm](http://www.gov.cn/gzdt/2010-08/12/content_1678211.htm)>. Access on: 30 Nov. 2010.

One official explanation is that the percentage of notifications involving multinationals is large because their annual turnover is sufficiently high to meet the filing thresholds.<sup>55</sup> While it is true that foreign companies have an oversized presence in many sectors, for the antitrust authorities this seems to pose more a threat to the growth of Chinese firms rather than to market competition. This is not only evidenced by the two-year AML enforcement record, with the arguably small sample of seven decisions, but by the existence of a preceding merger review system established in 2003 that only applied to foreign acquisitions.

Even assuming that all the seven decisions have been taken on valid competition grounds, the fact that not one M&A between Chinese firms has been the subject of adverse decision might bear testimony to the underenforcement of the current merger control regime. Over a hundred of “national champion” firms have grown substantially as a result of massive restructuring such as M&As in the most important industries that the state still monopolizes.<sup>56</sup> Given that the number of mergers between Chinese firms notified to MOFCOM is not publicly known, it is hard to assess the agency’s approach. But some of those transactions that meet the mandatory notification requirement are not even notified to MOFCOM. A particularly notable case in this category is the merger between China Unicom and China Netcom in October 2008, two of China’s leading telecommunications companies.<sup>57</sup> In this context, the more effectively the merger control rules are applied to foreign companies, the more the system is skewed in favour of domestic firms, especially the SOEs.

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<sup>55</sup> CHINA. Ministry of Commerce of the People’s Republic of China. Anti-monopoly Bureau. The transcript of the questions and answers during this press conference. *supra* note 53. Available at: <[http://www.gov.cn/gzdt/2010-08/12/content\\_1678211.htm](http://www.gov.cn/gzdt/2010-08/12/content_1678211.htm)>. Access on: 30 Nov. 2010.

<sup>56</sup> For example, see ECONOMY WATCH. *China advertises globally for national champion CEOs*. Available at: <<http://www.economywatch.com/in-the-news/china-advertises-globally-for-national-champion-ceos-19-09.html>> Access on: 30 Nov. 2010).

<sup>57</sup> RELATED news release. Available at: <[http://www.cs.com.cn/ssgs/02/200809/t20080917\\_1587421.htm](http://www.cs.com.cn/ssgs/02/200809/t20080917_1587421.htm)>. Access on: 30 Nov. 2010.

In summary, from its inception, China's merger control regime has been shaped by considerations and priorities unique to its stage of economic development. As a large emerging economy, China has benefited tremendously from foreign investment over three decades, which at the same time contributed to a market structure in which foreign companies dominates many sectors *vis-à-vis* fledging local firms. Chinese authorities appear to have first designed a merger review system specifically to address this concern and subsequently applied neutral AML provisions more aggressively to foreign multinationals. This obviously is not only of great concern to foreign investors interested in China's market, but also will have significant long-term impact on China's evolving antitrust law, the overall legal system, economic development and further integration with the world.

## **O regime do controle de fusão da China em face da integração global: características e implicações**

### **Resumo**

Desde que o regime do controle de fusão da China foi estabelecido pela Lei Anti-Monopólio (AML) em 2008, o resultado da aplicação desta lei causou uma preocupação crescente, pois o sistema seria inerentemente contrário às empresas multinacionais estrangeiras. Este artigo realiza uma análise da evolução do sistema de controle de fusões na China, avaliando seu papel e suas implicações. O desenvolvimento econômico constante da China, abastecido principalmente pelos investimentos estrangeiros, conduziu a um mercado interno caracterizado por uma forte presença estrangeira. A concorrência estrangeira e nacional tornou-se assim um assunto de relevância para os responsáveis políticos, especialmente em antecipação da entrada da China na Organização Mundial do Comércio. Esta preocupação precipitou o estabelecimento, em 2003, do primeiro sistema de revisão de fusões, o qual aplicava-se somente às fusões e aquisições por e entre empresas estrangeiras. Embora a Lei AML em princípio se aplique tanto em relação às empresas estrangeiras quanto às empresas chinesas, as autoridades reguladoras intervieram somente em aquisições estrangeiras. O regime de controle de fusão da China é diferente dos regimes das economias de mercado amadurecidas e tem

implicações significativas para si mesmo assim como para os investidores estrangeiros.

**Palavras-chaves:** China. Controle de fusão. Integração global. Concorrência nacional e estrangeira.

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